

NOV 17 1981

Gentlemen:

We have considered your application for recognition of exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code.

Your primary activity is the operation of the [REDACTED] beauty pageant. This pageant is preliminary to the [REDACTED], which is part of the [REDACTED]. Your funds are from the sale of advertising, sale of sponsorships to local businesses, and the sale of pageant tickets. Expenditures are primarily for pageant expenses, entertainment, supplies, advertising, clothing and accessories, and granting scholarships to winners and finalists.

Contestants in the pageant are required to sign a contract specifying her rights and duties as a possible winner. Winners are required to perform certain services for your organization such as personal appearances on behalf of businesses sponsoring the pageant. In the event that a winner of the pageant fails to carry out all her obligations, it would appear that all awards and scholarships must be returned.

Contestants must agree that, if they are the recipient of one of the [REDACTED] scholarships, they will permit their name, photographs, pictures, endorsement rights and title to be used by scholarship sponsors and they must not endorse in any way products competitive to those products of the scholarship sponsors.

Section 501(c) of the Code describes certain organizations exempt from Federal income tax under section 501(a) and reads, in part, as follows:

"(3)Corporations, \*\*\* fund, or foundation, organized and operated exclusively for religious, charitable, scientific, \*\*\* literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involved the provision of athletic

Code	Initiator	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer	Rev

facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office."

Section 1.501(c)(3)-1 of the regulations provides, in part, as follows:

"(a)(1) In order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt."

"(c)(1) Primary activities. An organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose."

Revenue Ruling 68-20, 1968-1 C.B. 55, deals with the Federal income tax treatment of various amounts received by a taxpayer who participates in and wins a contest. The contest is a national beauty contest and pageant conducted by a profit making organization. The contestants are required to sign a contract fixing her rights and duties as a participant in the national contest, as a possible national finalist, and as a possible national winner. The winner is entitled to receive a 4-year "scholarship" to the college of her choice. Under the circumstances, the "scholarship" is compensation to the contest winner for participation in the contest, for playing a leading role in the televised pageant, and for performing subsequent services for, and at the direction of, the corporation.

In Georgia Scholarship Fund, Inc., 72 TC 267, Dec. 85, 1979, the court held that a nonprofit organization operated for the purpose of giving scholarships to contestants entering a state beauty pageant was not an exempt organization. The scholarships were awarded only if certain contractual obligations were assumed by the contestant, a compensatory and not tax-exempt purpose.

Based on the information you have furnished, we have determined that you do not qualify for tax-exemption under section 501(c)(3) of the Internal Revenue Code. The scholarships you award are actually compensation for meeting required contractual obligations as directed by pageant officials, often for commercial purposes, and are not grants to carry out a charitable purpose. Accordingly, tax-exemption under section

501(c)(3) is denied and you should file Federal income tax returns.

If you do not agree with these conclusions, you may, within 30 days from the date of this letter, file in duplicate a brief of the facts, law, and argument that clearly sets forth your position. If you desire an oral discussion of the issue, please indicate this in your protest. The enclosed Publication 892 gives instructions for filing a protest.

If you do not file a protest with this office within 30 days of the date of this report or letter, this proposed determination will become final.

If you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7422(b)(2) of the Internal Revenue Code provides in part that, "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Court of Claims, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service."

If this determination letter becomes a final determination, we will notify the appropriate State Officials, as required by section 5104(e) of the Code, that based on the information we have, we are unable to recognize you as an organization of the type described in Code section 501(c)(3).

If you agree with these conclusions or do not wish to file a written protest, please sign and return Form 6018 in the enclosed self-addressed envelope as soon as possible.

If you have any further questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Sincerely yours,

  
District Director

Enclosures:  
Publication 892  
Form 6018